Do Tax Increment Finance Districts in Iowa Spur Regional Economic and Demographic Growth?

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Overview

This is a short report about tax increment financing in Iowa. It is based on a more detailed review of the topic, and readers interested in that research are encouraged to contact the authors.[*] The analysis summarizes the growth in tax increment financing as a mechanism for funding or setting the stage for economic development over the years. In so doing, it looks at the growth in tax increment finance districts over the years and measures whether that growth has indeed been instrumental in community and regional economic, demographic, and fiscal change. This report is a more focused description of the findings.

Our original research yielded these observations and conclusions:

- The ease with which TIF district designation can be done in Iowa, along with the multiplicity of uses that TIF districts can be put, has resulted in a law that has become a *de facto* entitlement for new industry and housing development in much of the state given the phenomenal rise in TIF districts over the past decade and the apparent ease with which the designations can occur.
- Iowa's counties are specifically burdened by this practice, as they primarily depend on property taxes for the preponderance of county-level services.
- Iowa schools are held partially harmless, as state aid kicks in to offset the erosion in tax base that would occur because of TIF accumulation among the cities. The state offset for the schools is not complete, but it is substantial. A state that now finds its accounts severely stretched may not continue to tolerate this shift.
- Evidence suggests that there is a high rate of subsidization of retained and new jobs and retained and new population in much of the state when compared to current TIF district spending. Stated differently, existing taxpayers, its householders, wage earners, and retirees are aggressively subsidizing business growth and population via this practice.
- We found virtually no statistically meaningful economic, fiscal, and social correlates with this practice in our assessment; consequently, the evidence that we analyzed suggests that net positions are not being enhanced – that the overall expected benefits do not exceed the public's costs.

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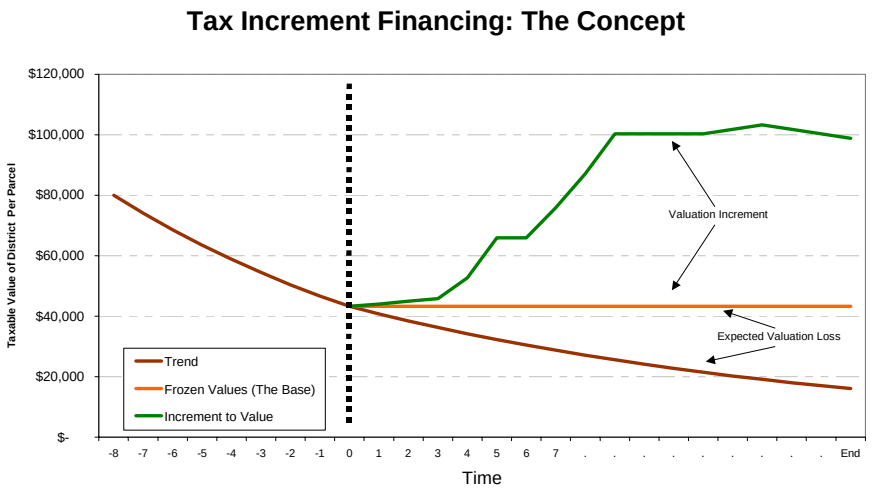
[*] Swenson, David and Liesl Eathington, "Do Tax Increment Finance Districts in Iowa Spur Growth or Squander Public Resources." Department of Economics, Iowa State University, April 2002.

Tax Increment Financing

Tax increment financing (TIF) has been around for decades as an economic development tool, though its potential and popularity didn't truly emerge for local officials until the late 1970s. The practice is conceptually simple: an area that has been blighted or is otherwise in need of an economic boost is designated, usually by a city, to be a tax increment finance district. The taxable value of that district is then frozen to the value it was on the day of the declaration. The frozen value is usually called the *base*. All jurisdictions that had taxing authority over the newly-formed TIF district still have taxing authority over the base. The city then prepares the district for development. As the district develops commercially, the incremental value of taxes *that would have been collected* by all of the taxing authorities is retained by the city to pay off the costs of readying the district for development. This new value is generally called *the increment*. Over time, when all of the public investment costs are paid off, the incremental taxable values are released back to all of the taxing jurisdictions who are then able to capture the new taxable value increment for their general funds.

We illustrate the concept in Figure 1. Here we see that the value of the average parcel of land in a hypothetical area of scrutiny is declining, and it is expected to continue to decline. The city decides to act. It declares a TIF district (at year zero). The base values are frozen, thereafter, as represented by the horizontal line. That is the tax base available to the city and all of the other taxing jurisdictions (county, school, community college, special districts, etc) for use in their general funds. The valuation increment (the rising line) ostensibly grows over time—perhaps slowly at first, but then more rapidly as the site is more fully developed and more industry, commerce, and residential investments are attracted. This generates the increment to tax revenues to pay off public indebtedness associated with the project, as represented by the distance from the base, horizontal line and the increment line over time. At the end point, all of the increment is released to all taxing jurisdictions, and all taxing jurisdictions get to capture the new taxable wealth. The supposition is that after taking the initial risk, all of the districts will now be better off than they would have been had no action been taken.

Figure 1



The process looks good on paper. The city declares an unproductive area a TIF district. It assumes the risk. Everyone else is held harmless, and if the trend is to be believed, the city is actually acting in all of their collective interests by taking action. Through their (the city's)

concerted and focused efforts new growth is spurred and the public realm as well as the private are enhanced.

Tax Increment Financing in Iowa

Like many states, Iowa's enabling legislation for a TIF district is rooted in urban renewal law. Procedurally, cities were first required to go through an urban renewal process. The statute originally, clearly, and solely applied to blighted areas, which were, according to Iowa statute, areas that

> … constitute a serious and growing menace, injurious to the public health, safety, morals and welfare of the residents of the state; that the existence of such areas … constitutes an economic and social liability imposing onerous municipal burdens which decrease the tax base and reduce tax revenues, [and] substantially impairs or arrests the sound growth of municipalities ….[1]

Changes to state law, however, in 1985 made economic development a general purpose activity and effectively eliminated the aforementioned grave language requiring a finding of blight, although the language has not been amended in the TIF statute; consequently, the preponderance of TIFs as evolved during the 1990s were for non-blighted, non-urban renewal types of developments. It is fair to assume that nearly all of the TIF districts in existence up to the end of the 1980s were of the original, urban renewal, blight-elimination variety, as they were aligned with the aforementioned statutory language. It is equally reasonable to assume that nearly all of the TIF districts that have been added in the state during the 1990s have been established for economic development purposes.

The state of Iowa has also expanded the allowable uses for TIF districts. A law was passed in 1996 that was designed to apply TIF incentives to the development of moderate and low income housing. That law was amended, however, the next year so that all value of housing be allowed in a TIF district, and the sponsoring city was required only to dedicate a portion of the TIF increment to promoting, enhancing, or otherwise stimulating low to moderate income housing anywhere in the community. These districts can only last 10 years, after which all of the increment reverts to all governments.

Iowa law allows for cities to borrow against the increment to fund improvements. Iowa law also allows the collecting city to simply rebate the taxes paid to the developer, homeowners, or the new industry *with or without* specific performance guarantees. In principle, once the TIF bonds are retired there is no reason for the district to remain in effect. Over the years there have been many TIF districts started, bonds let, improvements conducted, and districts released back to the tax base. There are also TIF districts that are more than 20 years old which have not been released back to the general tax base.

TIF Cities

Figure 2 displays much of the basic statistical information on TIF adoption by Iowa cities over the previous decade.[2] TIF nominal valuation in our cities increased from just under $650 million in 1989 to $4.2 billion in 1999 (Figure 2A), an increase of nearly 550 percent. All taxable valuation in our cities over this period increased by 53 percent, so the accumulation of TIF valuation by our cities was at a rate of more than 10 times greater than the overall growth in

[1] Chapter 403.2(1) Code of Iowa, 1999.

[2] In discerning characteristics of cities and TIF ordinances, we rely on the budget page of the "Adoption of Budget and Certification of Taxes" form required of cities by Iowa law, the collection of which is managed by the Iowa Department of Management.

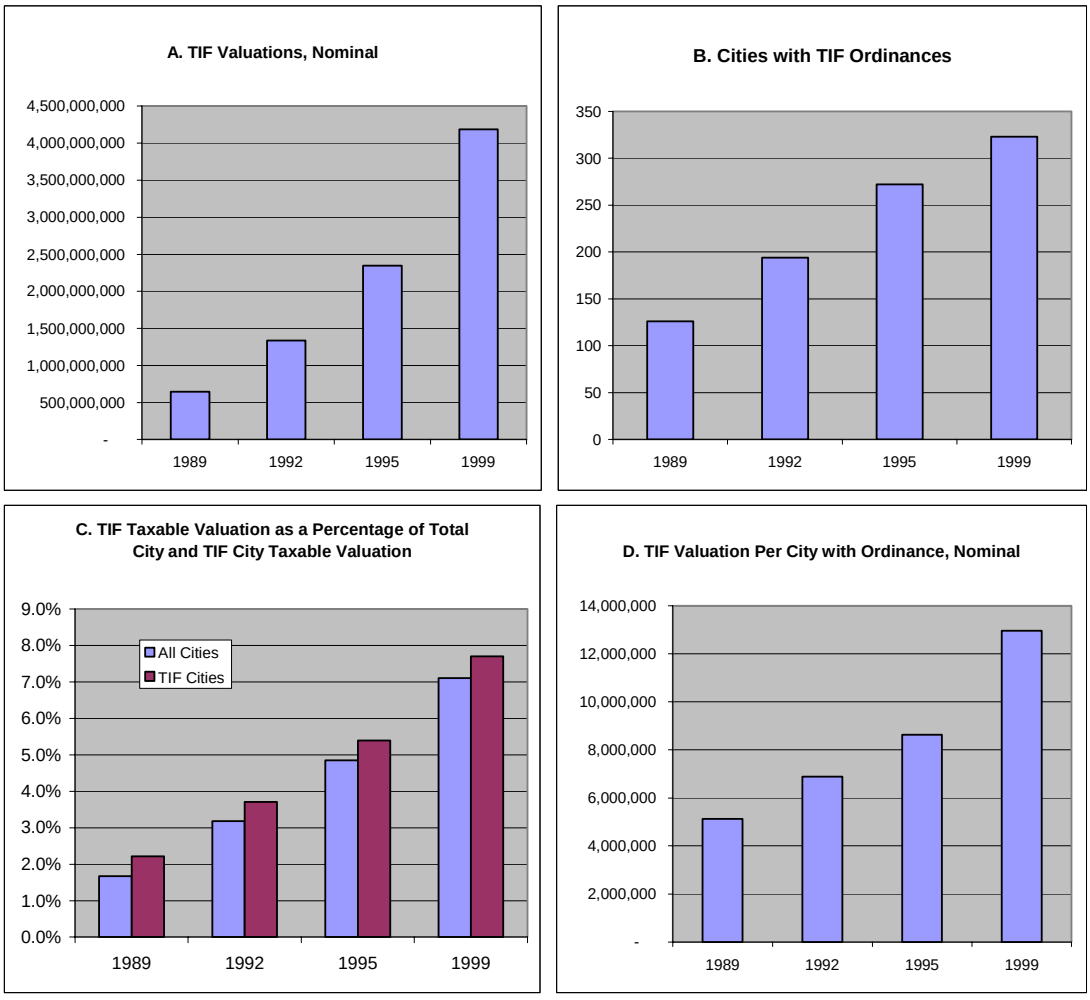
municipal taxable valuation. The number of cities with TIF ordinances also increased markedly over this period. In 1989 there were 126 cities (13 percent of the total number of cities) with TIF ordinances, by 1999, there were 323 (Figure 2B), an increase of 156 percent.

Figure 2C shows us the value of TIF valuation as a percentage of total taxable valuation in cities in the state and the total taxable valuation of cities that had TIF ordinances. In 1989, just 1.7 percent of the state's total city tax base and 2.2 percent of TIF city tax bases were in TIF districts. Those values steadily rose over the decade. In 1999, 7.1 percent of the state's city tax base and 7.7 percent of TIF city tax bases were in TIF districts.

This figure also underscores another factor: the 15 percent of cities that had TIF ordinances in 1989 accounted for 75 percent of the total taxable valuation available for cities. In other words, most of the 1989 TIF cities were quite large. By 1999, 34 percent of the state's cities have ordinances and the TIF cities accounted for 92 percent of the state's urban valuation. Stated differently, the 626 cities in Iowa that still did not have a TIF ordinance in 1999 accounted for only 8 percent of the state's urban tax base.

Figure 2D shows us the taxable value growth in our TIF districts over time. In 1989 the average taxable valuation (the increment) in TIF cities was $5.12 million. By 1999, that value had climbed to just under $13 million per city.

Figure 2. Indicators of Tax Increment Finance District Adoption in Iowa, 1989 to 1999



TIF Cities by Adoption Period and Metropolitan County

We reclassified the data in Figure 2 to help us to learn more about our communities that are using TIF ordinances. Nearly all of the communities that had TIF ordinances in effect in 1989 did so under the more strict, urban renewal and blight considerations.[3] Nearly all of TIF adoptions *after* 1989 did so without utilizing the urban blight criterion, as it was no longer a necessity in the law. We wanted, then, to distinguish what we could about these latter adopting cities in comparison to the earlier adopting cities. Finally, we wanted to take a look at some of the change characteristics of the 626 cities that have not enacted a statute. As the majority of economic growth in the state has accrued to its metropolitan counties, we also controlled for whether the city was in a metro county or not.

Figure 3 helps us to gain some perspective on our cities. In Figure 3A we see that the vast majority of both TIF and all other valuation growth between 1989 and 1999 has accrued to the original TIF cities, whether they were metro or nonmetro. The metro 1989 or before TIF cities added $1.4 billion in TIF value and $9.5 billion in all other value. The nonmetro 1989 or before TIF cities added a much higher ratio of TIF value ($964.1 million) compared to all other value ($3.56 billion). Although those cities adding TIF ordinances after 1989 yielded much less growth than our original group, we can see that the amount of TIF valuation as a percentage of all valuation is higher than the pre-1989 group. Valuation growth among our 624 non-TIF cities was very small, amounting to about $.864 billion in all.

Figure 3B gives us the changes per capita between 1989 and 1999 (using 1999 populations as the divisor). The metro pre 1989 cities added $1,506 per capita in TIF incremental values and $10,241 in all other values. The non-metro, pre-1989 cities added $1,576 in TIF increment and $5,585 in all other values. The metros here yielded nearly twice as much all other valuation growth as the nonmetros. Among the post 1989 cities, we see that those in the metros, primarily the booming suburban cities, averaged new TIF increment per capita of $3,563 and all other valuation of $11,500. For the post 1989 adopters that were not in a metro, they added $2,070 in TIF increment per capita and $4,048 in all other valuation. For this chart we can see that cities in the metropolitan counties fared much better in non-TIF valuation growth per capita than the other counties.

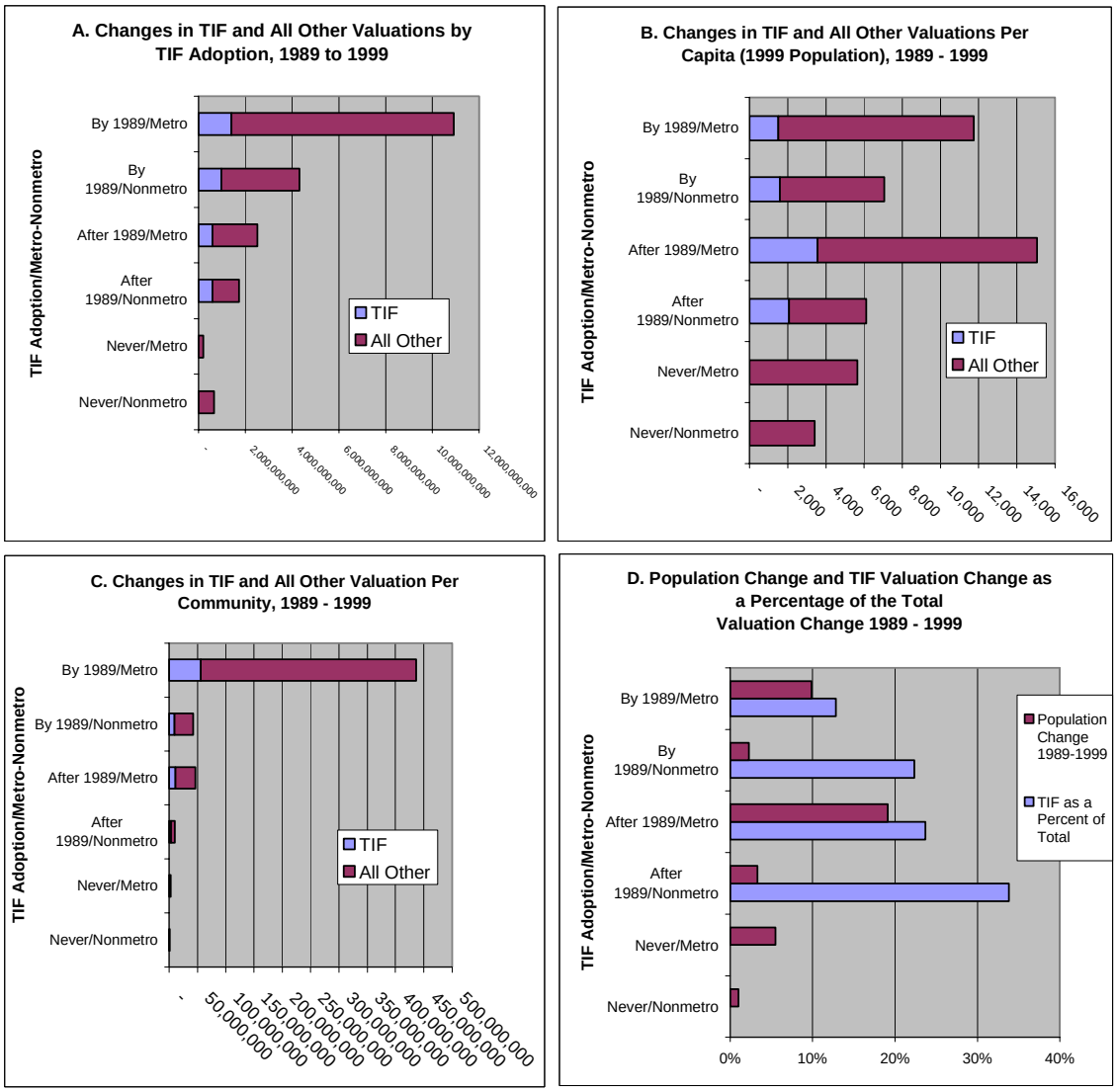
Figure 3C gives us the TIF increment and all other taxable valuation growth per community in each group. The accumulations in the metropolitan pre-1989 TIF communities were tremendously greater than the accumulations in all of the other sections. They added $55.98 million in TIF increment and $380.7 million in all other valuation per community over the period assessed. The nonmetros in this group added $9.5 million in increment and $33.3 million in all other taxable values. Per community, the metropolitan cities that enacted TIF statutes after 1989 did better then the nonmetro pre-1989 cities. They added $11.0 million in TIF increment per community and $35.5 million in all other valuation. The non-metro, post-1989 cities added $3.5 million in increment and $6.8 million in base per community.

Last, in Figure 3D we simply compare a couple of indicators. The first is TIF incremental valuation change as a percentage of total valuation change. The second is the percentage change in population over the same period. We can see that all of non-metro aggregations posted much lower population gains over the years measured than did their metropolitan aggregations. The metro, pre-1989 group grew by 9.9 percent, and the metro, post-1989 group grew by a whopping 19.1 percent. Among the nonmetro, after 1989 cities we find

[3] We have already established that the early adopters of TIF ordinances were the state's larger cities, including nearly all of its metropolitan cities and most of its larger trade centers. These were the cities that had undergone significant central city deterioration over the years and were the original candidates for renewal.

population growth 3.3 percent, and in the nonmetro pre-1989 cities we find population growth of just 2.3 percent. In both of these cases, these cities realized a lower rate of population growth than the cities located in the metropolitan counties that did not have a TIF ordinance in effect by 1999.

Figure 3. Major Changes in TIF Adopting and Non-Adopting Cities, 1989 to 1999



In contrast, when we look at TIF incremental values as a percentage of all taxable valuation growth for our cities, we see that for the post 1989 nonmetro cities, the TIF increment that they captured represented a full 34 percent of all valuation growth; among the metro post 1989 cities 24 percent of all new growth was captured in a TIF increment. The pre-1989 nonmetros captured 22 percent, and the metros in that group captured 13 percent. If we look at TIF capture as a measure of economic development effort intended to lead to job and population growth, at least by this measure the evidence indicates that the TIF "effort" only works, as measured by significant population gain, in metropolitan counties. Among our two nonmetropolitan city groups, we see each has a relatively high level of effort coupled with comparatively poor population performance.

Aggregating Outcomes at the County Level

The remaining data aggregate TIF characteristics at the county level so that we can compare the TIF data that we have to specific sets of economic, demographic, and broad fiscal measures that are, too, at the county level. The overall quality of data collection and the availability of data at the community level in Iowa is poor and does not allow for rigorous community level analysis. Remembering that 92 percent of the urban valuation is now contained within cities that have TIF ordinances in effect, our county level analysis captures that vast majority of valuation potentially influenced by TIF laws. It does not however, capture particular community-to-community differences.

Figure 4 gives an eye-opening display of the growth in TIF districts in the state of Iowa over the last decade. Our cities in metropolitan counties had 73 TIF districts in 1989, but by 1999 they grew to 673. Our cities in the state's nonmetropolitan cities had 112 districts in 1989, but they grew to almost 1,800 by 1999. If we compare this chart with the Figure 2A, we would see that in 1989 the average city with a TIF ordinance had 1.5 districts per city. In 1999 the average was 7.6 districts per city.

Figure 4. TIF District Growth, 1989 to 1999

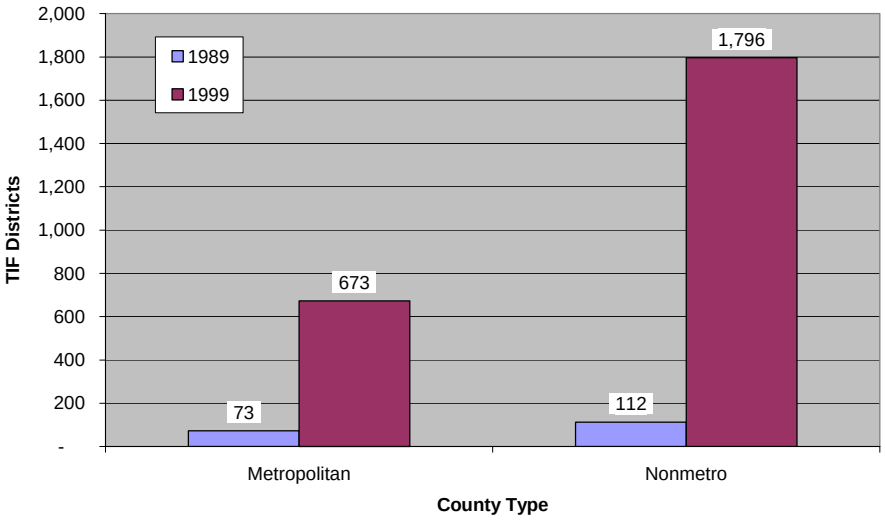


Table 1 displays the major fiscal changes in the TIF districts. Here we are comparing aggregate TIF valuations and incremental property taxes collected in our urban areas versus the remainder of urban valuation and property taxes.[4] By fiscal 1999, our TIF net valuation grew from $.721 billion to just over $4.0 billion, or by 456 percent. All other net valuation grew by 43 percent.[5] Concomitantly, TIF increment property taxes grew from $22 million to $118.8 million,

[4] An important clarification is in order. In Iowa, for tax purposes, all valuation located within boundaries of a municipal corporation is classified as "urban" – all other is classified as "rural." All cities are considered municipal corporations in the state whether their population is 15 or 205,000.

[5] "Net" valuation allows for the deduction of the exempted valuations and tax collections on residences attributable to military service.

or 442 percent.[6] For the urban remainder we see that taxes grew faster than the tax base: taxes grew by nearly 59 percent, while the base grew by just 43 percent.

Though we do not present the data here, our analysis also indicated that a growing fraction of the TIF incremental value came in the form of residential property. In 1989 it represented just 1.6 percent of the net TIF increment. By 1999, this property classification accounted for 24 percent of the incremental value, due mostly to the latter revisions in the law allowing TIFs for new residences.

Table 1. Changes in TIF and All Other Urban Valuation,1989 to 1999

		Net Taxable Valuation	Net Property Taxes
1989	TIF	721,186,298	21,940,107
	Urban Remainder	36,826,629,510	1,132,568,786
1999	TIF	4,007,702,629	118,827,467
	Urban Remainder	52,524,013,715	1,795,924,983
Actual Change	TIF	3,286,516,331	96,887,360
	Urban Remainder	15,697,384,205	663,356,197
Percentage Change	TIF	455.7%	441.6%
	Urban Remainder	42.6%	58.6%

TIF Correlations

Given the collective, wide-spread use of TIF financing among Iowa cities, one would expect sets of outcomes at the county level that would give us some indication of their success or not. The TIF ultimately is supposed to increase and enrich the tax base through job growth, population retention or growth, earnings gains, and trade enhancement. We have sets of variables in our analysis that allow us to isolate evidence of fiscal, economic, or social benefits attributable to the proliferation of TIF districts in our state.

TIF ordinance cities commanded about 92 percent of all urban taxable valuation across the state. In short, nearly all of the state's urban base is influenced to some degree by the presence of TIF districts. We have therefore aggregated our TIF fiscal statistics for urban territories to the county level.[7] To that data set we have added economic and population variables. Our simple method for analysis in this investigatory stage was to find the difference in shares in our TIF-based spending and other fiscal, economic, and social variables between 1989 and 1999 and calculate the Pearson's Correlation for them against the TIF spending variable.[8] If

[6] Our estimate of TIF property taxes is based on the weighted mean tax rate in each county less the offsets applied to each particular district (for example, general obligation bonding tax rates). Consequently, our calculations slightly underestimate tax collections at the county level.

[7] The data set that we rely on for this analysis is maintained by the state of Iowa and itemizes tax base and tax rate characteristics for each specific taxing jurisdiction in the state of Iowa. This data set allows for aggregation at the county level and by rural and urban area. It also allows for us to control for tax increment finance districts. This data set, however, is extremely difficult to aggregate to the community level as there are no specific community level identifiers.

[8] For the reader who is not statistically inclined, this is a measure of the correlation between two variables. A perfect correlation would yield a value of ±1.0, whereas a complete absence of correlation would yield a score of 0.0. A plus or minus sign tells the direction of the relationship: if it is positive, as one measure increases, so does the other; and if it is negative, as one moves up, the other moves down. Finally, as to the overall value of a measure, scores that are less than ±.30 are generally considered to be weak or minor relationships, those from ±.30 to ±.60 are considered small to moderate, and those ±.60 or greater are considered stronger or much more robust.

TIFs are, indeed, instrumental in maintaining regional fiscal, economic, and social vitality, then we would expect a positive correlation among our chosen variables against the TIF-increment spending. As the vast preponderance of new TIFs since 1989 were of the "bird in the hand" variety – directly associated with an industrial gain, we assume that there will be distinct measurable economic and fiscal outcomes. Our findings are presented in Table 2.

When we review the literature, the statutes, the logic, and practices of TIF adoption, we find that the TIFs are supposed to bolster the value of homes, the commercial and industrial base, ultimately the aggregate value of the remainder of the urban areas, and tax collections. These enhancements are expected to have a moderating or dampening effect on urban property tax rates. As TIFs were intended to attract better paying, usually manufacturing, jobs we would expect positive manufacturing job outcomes. As manufacturing jobs are highly sought and considered base jobs for any regional economy, we would expect concomitant multipliers to show up in nonmanufacturing jobs, as well. Ultimately, all regional jobs and earnings would rise, as would regional trade. Finally, with all of benefits of TIF-based incentives, we would expect positive population outcomes.

Table 2. TIF Increment Indicators versus Fiscal, Economic, and Social Variables

Correlates	TIF Tax Collections
Residential Market Values	0.019
Taxable Value of Commercial/Industrial	0.198
Net NonTIF Taxable Values	0.156
Net NonTIF Property Taxes	0.223
Property Tax Rate	0.084
Nonmanufacturing Jobs	-0.023
Manufacturing Jobs	0.254
All Nonfarm Jobs	-0.057
Nonfarm Earnings	0.139
Retail Trade	-0.095
Population	0.022

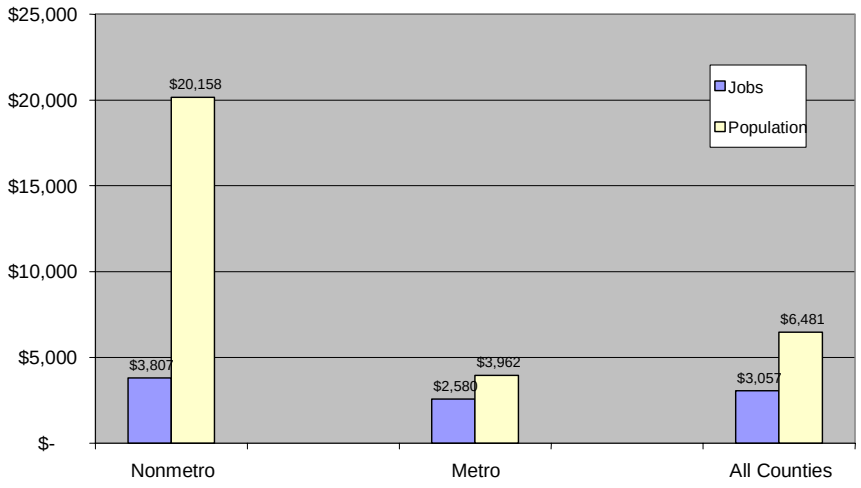
In the case of Iowa over the years that we have measured, 1989 to 1999, our change in shares of TIF-increment spending at the county level has not yielded important fiscal, economic, and social outcomes. Even though a growing fraction of TIF-increment spending is associated with new housing along with the still popular traditional manufacturing and other higher value economic enhancements, we found no correlation with the market value of homes. We do expect the increment to be funding more business and industry, which ultimately would show up as enhanced commercial and industrial taxable valuations. On a county-wide basis the correlation was quite small at less than r=.20. There was a positive, but relatively minor relationship between TIF-spending and nonTIF taxable property values (r=.16) and property tax collections (r=.22). These two correlations could represent a shifting of tax effort to nonTIF properties, or they could simply be associated with the larger places getting the growth, nonetheless; a situation that seems to be the case in the state. The positive rates of nonTIF valuation growth and tax collections, however, yielded no meaningful relationship between the change in TIF-spending and tax rates in our counties.

The strongest economic relationship found, though it is still very small, is in the share of manufacturing jobs at r=.25, which was expected as these are the kinds of jobs a TIF is typically used for. What was not expected, however, was how minor the correlation was. There is no statistically evident multiplier effect, either, as there was no correlation to speak of against nonmanufacturing jobs or all nonfarm jobs.[9] A very minor correlation was identified with nonfarm earnings (r=.14), and no relationship was found with retail trade or with population shares. As regards the current level of TIF-based spending in the state, their relationships to these sets of fiscal, economic, and population outcomes are truly under-whelming.

Conclusion

Where does this leave us? Figure 5, below, puts TIF spending into current perspective. First of all, the state of Iowa, over the period that we have scrutinized, enjoyed nonfarm job growth of about 320,000 but only yielded 150,000 more in population. Every county posted nonfarm employment gains, though the relationship between nonfarm job gains and population gains was uneven. Nonmetro counties enjoyed about 45 percent of the new job gains but only accumulated 12 percent of the new people. The values in Figure 5 represent the aggregate TIF spending in 2001 divided by the annual average increase in jobs and population, respectively, over the period that we assessed in this study. When plotted we find that in our nonmetropolitan counties, TIF spending per year amounts to $3,807 per new nonfarm job. In metro counties TIF spending is $2,580 per new nonfarm job.[10] Per new person, however, the spending outcomes are very high. In the nonmetros, the current level of TIF spending annually divided by the expected increase in population for this year is $20,158 per person. For the metros it is $3,962. Overall, statewide, current TIF spending per new job is $3,057 and TIF spending per new resident is $6,481. Relative to job and population yield, the costs of TIF activities in the state appear to be very high.

Figure 5. Current TIF Tax Collections by Annual Average Job and Population Increase, 1989-1999



[9] Though generally touted as a good thing, the expansion of manufacturing jobs in the state has on net yielded lower paying manufacturing jobs. In 1980, the average manufacturing worker in the state earned 105 percent of the U.S. average; in 1999 that same average worker made 83 percent of the U.S. average.
[10] This calculation is for all nonfarm jobs in the area. It is not possible to identify annual TIF spending per nonfarm job that is actually in the TIF districts from the data available to us.

The proliferation of TIF districts in Iowa and TIF-increment spending is intended to bolster the state's economic and population fortunes. Given the widespread adoption of TIF statutes (a third of all cities, within which 92 percent of the state's urban valuation is located) it is not possible to study our TIF cities with enough comparable control cities to determine both spatial and temporal efficacy. Consequently, we have been forced to simply try to isolate reasonable sets of correlates to see whether TIF increment spending in Iowa has led to discernible fiscal, economic, and social outcomes. We have determined that these measures do not yield significant positive outcomes for the state of Iowa and its tax payers. Indeed, as the last figure indicates, the state's primarily urban tax payers are heavily subsidizing job growth and population growth (assuming that is what the TIF districts are for primarily).

There are several issues to consider about TIF ordinances and TIF outcomes in Iowa. From our research here and from our larger study of the topic, it seems apparent that the ease with which TIF district designation can be done in Iowa, along with the multiplicity of uses that TIF districts can be put, that the law now has become a *de facto* entitlement for new industry and housing development in much of the state with little to no evidence of overall public benefit or meaningful discussion of the mean costs of the practice. It also seems apparent that given the ease with which these districts can be developed that many cities may be preemptively capturing new valuation and tax revenues in the name of economic development, but that in the main, this preemption is likely yielding much more collective fiscal harm across taxing districts in the long run than good. Iowa's counties are specifically burdened by this practice, as they primarily depend on property taxes for a large fraction of county-level services.[11] Iowa schools are held partially harmless, as state aid kicks in to offset the erosion in tax base that would occur because of TIF accumulation among the cities. The state offset for the schools is not complete, but it is substantial. One indirect outcome, then, is that a large portion of current TIF-based losses to local governments, schools in particular, is borne by state government, and that fraction has increased drastically over the last 10 years. One wonders if a state that now finds its accounts severely stretched will continue to tolerate this shift.

Finally we get to the "bird in the hand" problem when dealing with local officials. In a large fraction of TIF transactions across the state in recent years there is an actual company with actual jobs. There is a negotiation, perhaps for performance, i.e., roads, curb and gutter, a set number of new jobs, etc., or perhaps their taxes are simply rebated for just building in our town – sort of a selection reward. City officials believe that the TIF action was instrumental in job growth in their town and in their region. How could it not be? We have an investment, and we have a firm with jobs. On net, however, except for the increment to manufacturing jobs, there is no evidence of economy wide benefits (trade, all nonfarm jobs), fiscal benefits, or population gains. There is indirect statistical evidence that this profligate practice is resulting in a direct transfer of resources from existing tax payers to new firms without yielding region-wide economic and social gains to justify the public's investment.

This analysis suggests that the enabling legislation for tax based incentives deserves revisiting. Though the TIF programs is highly popular among city government officials, and why wouldn't it be given the growth in property tax yield over the years, there is virtually no evidence of broad economic or social benefits in light of the costs.

[11] We must note, however, that counties in the state have adopted an aggressive stance towards cities' practice of pre-emptive TIF adoption and TIF district extension. Some, especially the larger counties, are confronting the TIFing communities and demanding a share of the either accumulated increment or anticipated new increment on an extension. The communities are not obliged to do this, but given local politics and pressure have begun to negotiate payments in "lieu of taxes" to county governments.